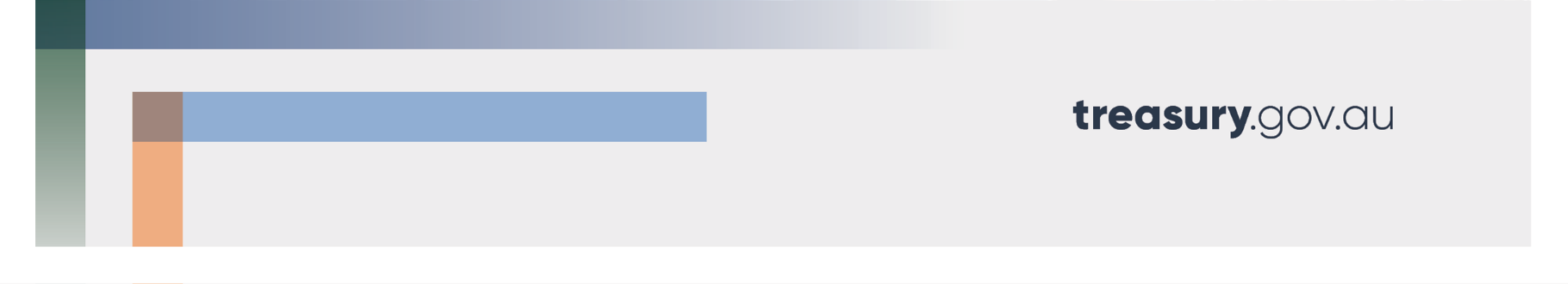
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Sustainable Finance Strategy

Consultation paper

November 2023



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# Consultation Process

## Request for feedback and comments

The Government seeks views on Australia's Sustainable Finance Strategy and the specific questions raised in this paper. These views will inform ongoing policy development and regulatory engagement on sustainable finance in Australia.

Closing date for submissions: 01 December 2023

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| Mail | Sustainable Finance Unit  Climate and Energy Division  The Treasury  Langton Crescent  PARKES ACT 2600 |
| Enquiries | Enquiries can be initially directed to the above email address. |

The principles outlined in this paper have not received Government approval and are not yet law. As a consequence, this paper is merely a guide as to how the principles might operate.

# Executive Summary

Australia’s transition to net zero will require a significant amount of private and public investment. It is important that financial markets are well placed to finance this transition and therefore support the Government’s emissions reductions target. To assist this financing, the Government has proposed an ambitious and comprehensive Sustainable Finance Strategy. The Strategy will help mobilise the private investment needed in coming decades, enable Australian firms to access the capital needed to finance their own transitions and take advantage of new opportunities that arise, and ensure that the financial opportunities and risks presented by climate change are identified and well managed. The Strategy also recognises that markets are increasingly focussed on sustainability issues that extend beyond climate change.

This Strategy proposes a range of measures to underpin the development of Australia’s sustainable finance markets (Figure 1). The foundation of the strategy is ensuring that markets have access to high-quality, credible and comparable information that will enable them to assess both the financial risks that climate change and other sustainability issues present to firms, and the impact of firms on the climate and environment (Pillar 1). This includes the Government’s climate-related disclosure regime and a sustainable finance taxonomy. At the same time, Australia’s financial regulators should be well supported in their efforts to address the impacts of climate change on businesses and the financial system (Pillar 2). Finally, the Government should take a leading role in supporting the development of sustainable finance markets and shaping international developments in sustainable finance markets (Pillar 3).

The range of policies recommended in this strategy would provide a strong foundation for sustainable finance in Australia and align Australia’s capital markets with emerging international standards.

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| **Figure 1: Summary of proposed priorities** | |
| **Pillar 1:**  **Improve transparency on climate and sustainability** | |
| Priority 1: Establish a framework for sustainability-related financial disclosures | Priority 2: Develop a Sustainable Finance Taxonomy |
| Priority 3: Support credible net zero transition planning | Priority 4: Develop a labelling system for investment products marketed as sustainable |
| **Pillar 2:**  **Financial system capabilities** | |
| Priority 5: Enhancing market supervision and enforcement | Priority 6: Identifying and responding to potential systemic financial risks |
| Priority 7: Addressing data and analytical challenges | Priority 8: Ensuring fit for purpose regulatory frameworks |
| **Pillar 3: Australian Government leadership and engagement** | |
| Priority 9: Issuing Australian sovereign green bonds | Priority 10: Catalysing sustainable finance flows and markets |
| Priority 11: Promoting international alignment | Priority 12: Position Australia as a global sustainability leader |

# Introduction

Australia’s financial system plays an integral role in aligning investment and economic growth with climate, environmental and social goals, including financing the transition to net zero.

In Australia and around the world, businesses, investors and policymakers are responding rapidly as climate-related opportunities and risks reshape financial markets, economies and societies, and impact the financial prospects of companies. Climate, nature and other sustainability issues are being integrated into core business practices, including corporate governance, capital allocation and risk management. Shareholders are demanding more sophisticated climate and sustainability strategies. Financial regulators are requiring firms and financial institutions to consider climate and sustainability as fundamental financial drivers of risk, returns and good governance, not peripheral considerations. Governments and communities are considering the role that businesses, investors and the financial system can play in mobilising the financing needed to achieve net zero goals.

These developments are part of a growing global focus on ‘sustainable finance’ – a term which describes financial flows that integrate consideration of impacts on society and the natural environment. This reflects a growing understanding of the role that the financial system must play to address global challenges, including climate change. It also recognises the need for financial system participants to manage emerging opportunities and risks to deliver long-term financial returns and support financial stability.

Consistent with global practice, the Government is adopting a ‘climate first’ approach to sustainable finance reforms. This reflects the systemic nature of climate-related opportunities and risks and the need for urgent responses. It also recognises that international efforts to embed climate opportunities and risks into finance are further advanced than other areas of sustainability. Through the Strategy, the Government also considers nature-related issues – reflecting rapidly growing investor expectations for greater transparency on nature risks and Australia’s interest in protecting natural landscapes, ecosystems and biodiversity (see Box 1).

Sustainable finance can be a significant competitive advantage for Australia in the global economy. At a minimum, Australia should have a robust regime that ensures Australian firms remain competitive in global capital markets. More ambitiously, it can leverage the strengths of our financial markets and offer opportunities to invest in the technologies and industries that will underpin a prosperous, low emissions future for Australia and our global partners.

While Australia’s private sector has led the way in responding to these shifts, there is a critical role for Government leadership. Setting clear policy targets, developing robust sustainable finance regulatory frameworks, and expanding catalytic Commonwealth investment will provide financial markets with the clarity, confidence and capabilities they need.

In December 2022, the Government announced that it would pursue a coordinated and ambitious sustainable finance agenda. This Sustainable Finance Strategy Consultation Paper outlines immediate investments and reforms that the Government has identified as most important for supporting sustainable finance in Australia, beginning with a focus on climate-related issues, but building frameworks that can expand over time. It seeks feedback on a broad range of reform options and priorities to establish a strong, long-term foundation for greater alignment between finance and sustainability goals.

# Objectives and structure

Sustainable finance touches on many areas of policy, regulation and the financial system. This Strategy focuses on the issues that are most critical for sustainability-related transparency, governance and credibility in financial markets. It will complement Australia’s wider climate, economic and environmental policy to provide consistency and clarity across the policy and regulatory frameworks that shape investment decisions across the economy. The Strategy has **three overarching objectives**:

This Strategy sets out key policy priorities structured in **three key pillars** to deliver on these objectives:

Within each pillar, the Strategy highlights key policy priorities and the Government’s proposed approach. Where relevant, it also highlights complementary priorities, initiatives and reform options.

After considering stakeholder feedback to this consultation paper, the Government will publish an implementation roadmap for the Sustainable Finance Strategy.

# Key principles

**Australia’s arrangements should be aligned with global markets and support two-way capital flows**

Maximising alignment with global frameworks for sustainable finance is necessary to ensure comparability and minimise compliance burdens and costs for Australian and international firms and investors. This should include consistency in the design of regulatory requirements or standards, recognising that in some cases divergence will be necessary to reflect Australia-specific economic and policy priorities.

**Australia should take a high-ambition approach**

To be effective, Australia’s sustainable finance arrangements must be aligned with science-based global climate and sustainability goals, and with Australia’s policy targets and commitments. They should encourage high-ambition approaches by firms, institutions and entities, including where these go beyond baseline standards established by regulation and policy. They should ensure that activities aligned with certain sustainability objectives do not undermine other sustainability goals.

**Australia’s strategy should support Australia’s emissions reduction plan and transition pathway**

The Strategy will seek to mobilise the private sector investment needed to support net zero, Australia becoming a renewable energy superpower and other sustainability goals. The Strategy should support investment in transition activities, as they are critical to ensuring our economy can effectively pivot to a low to zero emissions world, meeting our emissions reductions targets, and providing the critical resources and support needed for our region’s energy transition.

**The approach should be carefully staged and sequenced**

The Strategy will take a ‘building blocks’ approach. Reforms will be introduced progressively, beginning where needs are most urgent and policy options are more developed. Changes will be clearly communicated and consulted on to ensure entities can develop the capabilities needed to meet new regulatory requirements. While reforms will be staged, work will begin immediately to build the regulatory and market capabilities and infrastructure to support more ambitious responses over time.

**New requirements should be as simple and useable as possible for a wide range of actors**

Sustainable finance frameworks should make it simpler for firms to report opportunities and risks, back up sustainability claims, and pursue sustainability-aligned investments. They should also make it easier for individual shareholders and decision makers to access, understand and act on sustainability-related information. Where complex regulatory arrangements are required, these should be proportional to need and aligned as far as practical with existing regulatory thresholds, frameworks and models.

**Efforts should begin with climate and progress to other environmental and social priorities**

Climate should be the first priority for sustainable finance, but reforms should provide a platform to incorporate other critical sustainability-related issues over time. This should include a special focus on our natural capital and biodiversity, as well as incorporating First Nations perspectives and supporting positive social and economic outcomes for First Nations people.

**Collaboration and shared responsibility should be at heart of our approach**

Efforts to better align our economy and financial system with shared sustainability goals will require cooperation and partnership across community, business, investors and policymakers. Reforms to promote sustainable finance should be genuinely collaborative and consultative. Where possible, the Strategy should promote co-development of new frameworks and models for cross-sector collaboration.

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| **Box 1: The role of nature and biodiversity within the Strategy**  The Government is incorporating nature and biodiversity in the Strategy and aligning financial flows with nature-positive outcomes. Climate change is a key driver of nature and biodiversity loss, and these natural assets and services play a critical role in climate change mitigation and adaptation. Recognising that the investment required to meet global nature‑related targets and goals is less than the anticipated economic cost of biodiversity loss, capital must be urgently mobilised toward nature-positive investment. Responding to these issues is an increasing focus of firms, investors and regulators.  Australia is a signatory of the Kunming-Montreal Global Biodiversity Framework (agreed December 2022) and has committed to ambitious goals and targets within the framework. This includes the alignment of private sector financial flows toward activities that benefit nature and support businesses to assess and disclose nature-related opportunities, risks and dependencies.  This Strategy includes several nature-related priorities across its key pillars and reform proposals.  **Transparency**  Key frameworks for sustainability-related transparency and reporting will be designed in a way that allows for expansion to nature-related issues over time. This will include:   * Ensuring legislative changes to deliver climate disclosure reforms provide flexibility to expand to nature-related financial disclosures over time as global standards mature. * Incorporating nature-related ‘do no significant harm’ provisions during the initial phase of taxonomy development, and assessing how nature and biodiversity objectives can be incorporated into the taxonomy once climate mitigation criteria have been delivered.   **Capability**  Increased recognition of nature as a driver of firm-level and systemic opportunities and risks will be reflected in regulatory guidance, supervisory practices and data initiatives. This includes:   * Australian Securities and Investments Commission (ASIC) considering how regulatory guidance could support voluntary nature-related disclosures and nature-related claims for investment products. * The Council of Financial Regulators (CFR) Climate Working Group building its capacity to analyse and respond to nature-related financial risks, including through global regulatory initiatives and knowledge sharing. * The Government continuing to strengthen data frameworks and resources for assessing nature-related risks and measuring natural capital.   **International engagement**  Leadership on nature, including biodiversity and ecosystems, will be an important focus for Australia’s global engagement on sustainable finance. This will include:   * Continuing to support the work of the Taskforce on Nature-related Financial Disclosures (TNFD) as a key strategic partner. * Supporting work towards a consistent global baseline for nature reporting through the International Sustainability Standards Board (ISSB) in the medium-term. * Supporting a focus on nature-related investment opportunities, risks, and capabilities in our bilateral and regional engagement on sustainable finance. |

# Pillar 1: Improve transparency on climate and sustainability

Transparency is a fundamental feature of efficient financial markets. This expectation is deeply embedded in Australia, supported by financial reporting requirements and other disclosure obligations.

In recent years, sustainability has become a critical consideration in financial markets. Corporate climate and sustainability policies and targets are more ambitious; the financial opportunities and risks associated with sustainability trends are more material; and appetite for climate and sustainability‑aligned investments and business practices is significant and growing. Globally there is increased focus on supporting firms to better understand, manage and disclose how sustainability and climate-related financial opportunities and risks impact their financial performance and prospects – consistent with the approach to other material financial risks. There is also greater attention on how business and investment activities impact wider sustainability trends and goals, and recognition that these impacts can also create opportunities and risks for firms and institutions to manage.

Improving the transparency and consistency of sustainability and climate-related information is the foundational priority for this Strategy. The Government’s ambition is to support a marketplace where sustainability-related risks, opportunities, impacts and plans can be identified clearly, communicated confidently, and readily compared and understood.

The Strategy has identified four key priorities as critical building blocks for improving transparency:

* Ensuring standardised **disclosure of climate and other sustainability-related financial opportunities and risks** – starting with implementing mandatory climate reporting requirements will provide a strong foundation for more transparency across the financial system.
* Developing an Australian **sustainable finance taxonomy** – to provide a comprehensive medium‑term framework for market participants to understand how certain economic activities and investments align with, or contribute to, good sustainability outcomes.
* Supporting **credible climate transition planning and target setting** – recognising the critical importance of the net zero transition as a driver of opportunity and risk for Australian entities and our economy.
* Improving **sustainability labelling for investment products** – to provide more consistent information on the design and sustainability characteristics of products labelled as ‘green’, ‘sustainable’, ‘ESG’ or similar.

Australia’s proposed approach is consistent with steps being taken in other jurisdictions. Ensuring international alignment and supporting the consistency and interoperability of emerging global transparency frameworks will be a key focus for Australia.

## Priority 1: Establish a framework for sustainability-related financial disclosures

To support informed investment decisions, financial market participants need comprehensive and comparable information on financially material sustainability-related opportunities and risks. Increasingly, shareholders, investors and regulators expect sophisticated and standardised reporting of this information. The Government has already committed to introducing internationally-aligned and standardised, mandatory climate-related financial disclosure requirements for large businesses and financial institutions (climate disclosure reforms).

Internationally, work is well progressed to develop frameworks that define what is financially relevant sustainability information and how this should be disclosed. In June 2023, the ISSB released the new global baseline for sustainability- and climate-related disclosure standards for for-profit companies and financial institutions. This work was informed by the Task Force on Climate-related Financial Disclosures (TCFD) recommendations from 2017.

Climate disclosure reforms are central to this Strategy. They will provide the key building block to support strong climate information flows in financial markets, providing a foundation for broader regulatory reforms including enhanced transition planning expectations, the design of the taxonomy, and investment product labelling requirements.

Over time, global sustainability disclosure expectations will extend beyond climate as investor demand for sustainability information continues to grow and broaden. The TNFD released its recommendations for the disclosure of financial risks related to the loss and degradation of nature in September 2023 (see Box 1). The ISSB has indicated that this work is expected to provide the foundation for development of international nature-related financial disclosure standards over time.

The Government will continue to closely monitor international developments on sustainability disclosure frameworks. Expanded sustainability disclosure requirements in Australia will be considered as international standards emerge, consistent with the commitments Australia has made to support global efforts to strengthen nature and biodiversity related reporting. In the meantime, ASIC will consider updating guidance in relation to voluntary nature-related disclosures, as it did for climate disclosures in 2019.

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| Proposed approach  The Government is implementing mandatory climate-related financial disclosure requirements for large companies and financial institutions. These reforms are proposed to commence for reporting periods starting 1 July 2024 for the largest listed and unlisted companies, with others phased in over time.  The Government is closely monitoring the development of other international sustainability-related financial disclosure frameworks and standards, with a view to establishing other globally-aligned sustainability-related financial disclosure requirements (including nature) over time. |

**Developing mandatory climate-related financial disclosure requirements**

In June 2023, Treasury commenced its second consultation process, which sought views on a detailed design proposal for the new mandatory disclosure requirements. Feedback from this consultation will inform the Government’s decisions on implementation, including required legislative changes.

Following the release of the ISSB standards, the Australian Accounting Standards Board (AASB) will develop Australian climate disclosure standards, in line with the ISSB’s *IFRS S2 Climate*-*related Disclosures* standard, with modifications as necessary for the Australian context.

Treasury will work with regulators, industry, and other stakeholders to ensure Australian entities are well placed to meet new requirements. Government is seeking feedback on opportunities to support capacity building, including education, guidance or resources that would support high quality disclosures, particularly in areas such as scope 3 emissions reporting and scenario analysis.

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| For feedback   * What are the opportunities for Government, regulators and industry to support companies to develop the required skills, resources and capabilities to make climate disclosures under the proposed new obligations? * How should the Government, regulators and industry prepare for global developments in sustainability-related financial disclosure frameworks and standards, including the TNFD? |

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| Box 2: Climate disclosure in the public sector  Governments and public sector entities are also subject to climate-related opportunities and risks. As markets and regulators demand more comprehensive disclosures by companies, it is important that similar requirements apply to comparable public sector entities. This will support planning and risk management and build community confidence that these risks are being managed by public authorities and policy makers.  The Government has committed to introduce climate disclosure requirements for Commonwealth entities commensurate with the Government’s commitment for the private sector. These will enhance climate opportunity and risk disclosures across the Commonwealth public sector and ensure market neutrality between the private and Commonwealth public sectors is maintained.  Some large Commonwealth companies that meet the proposed thresholds for inclusion are proposed to be captured under the proposed private sector reforms. It is proposed that other Commonwealth entities that do not fall within these thresholds will also be subject to the commensurate disclosure requirements set by the Minister for Finance.  At the Commonwealth level, the Government has outlined climate risks as part of the wider statement of risks in the Budget papers. The 2023 Intergenerational Report also included a detailed assessment of long-term climate risks and impacts facing the Australian budget and economy. In addition, the Minister for Climate Change and Energy is leading the development of a new Climate Risk and Opportunity Management Program (CROMP), to support Commonwealth agencies to evaluate and prioritise management of climate risks.  In October 2023, the Minister for Finance, Senator the Hon Katy Gallagher, released new rules to require the Future Fund Board of Guardians to periodically disclose its investment holdings. |

## Priority 2: Develop a Sustainable Finance Taxonomy

The type of information needed by market participants is evolving as the focus on sustainability in global financial markets grows. In addition to disclosure of sustainability-related financial opportunities and risks, firms, investors and regulators are increasingly demanding more consistent and credible information about whether particular assets, activities or industries are aligned with the transition towards net zero and other sustainability goals.

Providing this information in a consistent way has been challenging. Metrics, data and standards used to substantiate sustainability impacts vary substantially across different firms and markets. There are few widely accepted frameworks for providing credible assessments of sustainability alignment, and the best economic and scientific basis for making these judgements is often heavily contested.

This lack of clarity limits the flow of sustainable finance and the ability of financial markets to support sustainability goals. Inconsistent or inaccurate information about sustainability alignment creates costs and distortions, impeding the efficient allocation of capital towards the activities that support good sustainability outcomes. The absence of common understanding and clear definitions increases risks of greenwashing and undermines investor confidence in sustainable finance. This is especially critical to avoid at a time when sustainability-themed investment is surging, and financial markets have an indispensable role to play to make net zero and other sustainability goals achievable.

In light of these challenges, taxonomies have emerged as a critical part of market and regulatory architecture for sustainable finance globally. Sustainable finance taxonomies provide consistent, scientifically rigorous criteria to evaluate whether economic activities are aligned with or contribute to climate and other sustainability outcomes (see Box 3). Over 20 jurisdictions have introduced or are developing sustainable finance taxonomy frameworks.[[1]](#footnote-2)

At the 2023-24 Budget, the Government announced that it would partner with industry to support the initial development phase of an Australian sustainable finance taxonomy in 2023 and 2024, with a view to taking ownership of taxonomy development and establishing a taxonomy as a key foundation for Australia’s wider sustainable finance landscape in the longer term. An Australian taxonomy will support international alignment and interoperability with other sustainable finance frameworks and taxonomies, and serve as a key foundation for Australia’s sustainable finance landscape.

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| Proposed approach  The Government is supporting the development of an Australian sustainable finance taxonomy as a key foundation of this Strategy, with an initial focus on climate mitigation objectives.  An Australian sustainable finance taxonomy should:   * Support the mobilisation of private capital towards sustainable activities * Provide a foundation for further regulatory measures to address greenwashing, such as sustainability disclosures by firms and issuers of investment products * Be developed in a collaborative manner between Government and industry, with strong governance arrangements * Be credible and science-based * Effectively incorporate a role for transition finance * Develop criteria for climate objectives first, while establishing a foundation to expand to other sustainability objectives (such as nature and circularity in the economy) * Include a robust approach to ‘Do No Significant Harm’ * Have an overarching focus on practicality, useability and international operability.   As they are developed, taxonomy criteria will provide an important source of guidance and consistency for firms, investors and regulators, improving transparency and supporting the development of credible sustainable financial products.  During the initial development phase of the taxonomy, the Government will make further decisions on the potential regulatory use cases for a taxonomy. In particular, this will consider how taxonomy criteria could be incorporated into corporate reporting requirements, transition planning frameworks, and labelling schemes for sustainable investment products.  Once established, the taxonomy should be maintained by an appropriate government body to ensure that it is effectively embedded in Australia’s regulatory framework. |

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| Box 3: Sustainable finance taxonomies  A sustainable finance taxonomy is a set of criteria which can be used to evaluate whether economic activities are aligned with or contribute to climate and other sustainability objectives. They can be used by investors to assess the extent to which an investment in an activity, entity or asset would support sustainability objectives and outcomes. Key features of a taxonomy include:  ***Policy objectives:*** A common policy objective is to support mobilisation of capital toward sustainable activities with an initial focus on climate change, and/or to assist regulators address greenwashing.  ***Sustainability objectives:*** Sustainability objectives can include outcomes, targets, goals relating to climate, nature, circular resource use, pollution, social objectives and other goals.  ***Science-based technical screening criteria (TSC):*** The underlying criteria and definitions used in a taxonomy depends on the sustainability objective(s) chosen and are typically science-based. For example, a taxonomy focused on climate mitigation would have technical screening criteria that set thresholds for a level of emissions or energy efficiency that need to be met for a certain activity or asset to be classified as taxonomy-aligned and therefore sustainable.  ***‘Do no significant harm’ provisions:*** This principle means that alignment with one sustainability objective is not enough for an activity to be regarded as sustainable if the activity causes significant harm under another objective.  ***Treatment of transition:*** Some taxonomies are entirely ‘green’, i.e. they only include activities that are already at very low or no carbon emissions, whereas others include activities that are in “transition” or enable a transition to lower emissions. |

**Developing the taxonomy and overseeing the initial development phase**

The initial development phase of a sustainable finance taxonomy will be led by the Australian Sustainable Finance Institute (ASFI) with oversight provided by the CFR Climate Working Group. This process will accelerate the technical and institutional foundations for an Australian taxonomy while the Government consults with industry on the wider elements of this proposed Sustainable Finance Strategy. The key output will be a set of preliminary taxonomy criteria for assessing how activities are aligned with climate mitigation objectives for key Australian economic sectors.

To support its work, ASFI is convening a Taxonomy Technical Expert Group (TTEG) that represents both the financial sector and the real economy, contracting expert advisers who have helped developed taxonomies in other jurisdictions, and organising sectoral stakeholder working groups to ensure wide consultation. As part of its oversight role, the CFR Climate Working Group has provided a Term of Reference to ASFI for this development phase that outlines the role of ASFI and the TTEG, and will regularly review ASFI’s progress and outputs to ensure they are aligned with the Government’s policy objectives. Further information about the workplan, governance and priorities for the initial development phase, including the oversight role performed by the CFR Climate Working group, is available at [ASFI’s website](https://www.asfi.org.au/taxonomy).

**Incorporating transitional activities and investments in an Australian taxonomy**

Some international taxonomies focus primarily on activities that already have very strong “green” or “sustainable” characteristics – setting a high bar for activities considered to be aligned with the taxonomy. However, many include other activities or technologies which are necessary to support the transition to net zero in the short to medium term, and therefore require continued investment and financing, even if they are not consistent with net zero or other goals in the long term. This acknowledges that the transition to net zero will require some ongoing investment in higher-emitting activities that have credible pathways to reduce emissions and/or provide critical inputs to more sustainable products, activities and industries. Defining which activities are consistent with transition involves complex scientific assessments, and difficult judgments about the policy, sectoral and technological mix that can drive progress to net zero.

As an emissions-intensive economy with major renewable energy potential and significant resources‑related trade and investment flows, transitional activities and investments will be critical to Australia’s future prosperity, its ability to meet net zero, and managing a just transition. A taxonomy that provides rigorous, science-based criteria to define activities that can credibly support the transition – and on what timeframes – will provide clear and credible guidance for firms, investors and regulators and a mechanism for measuring progress and increasing ambition over time.

The development phase for the taxonomy will assess the most promising options for incorporating transition into an Australian framework. This will draw on industry-led scoping exercises, input from the CFR Climate Working Group, and consultations with other jurisdictions and technical specialists to draw on global experience. Further, the transitional aspects of the taxonomy will be aligned where possible with sectoral plans developed by the Climate Change Authority (CCA) and across government to maximise consistency with whole-of-government pathways.

**Regulatory use cases for an Australian taxonomy**

Taxonomies are tools to support consistent standards and information flows and support sustainability-aligned investment decisions by firms and markets, rather than to mandate particular investment approaches or dictate capital allocation decisions. Once established, taxonomy criteria can be adopted and applied voluntarily by firms, institutions and regulators to help assess sustainability-related performance, investment allocation, risks and representations. They can also be embedded directly in financial regulatory architecture in a range of ways, as part of more active steps to improve the quality and consistency of information available to markets and consumers. Box 4 provides examples of use cases for taxonomies internationally.

During its initial development, Australia’s taxonomy will have no formal regulatory status – although it is anticipated that it will provide important and influential guidance to market participants. However, Treasury and the CFR will consider options for embedding the taxonomy in Australia’s regulatory architecture, where doing so can promote greater transparency and consistency in sustainability-related disclosures, financial products and markets. Medium-term options include:

* **Requiring large firms to disclose the degree of alignment of their activities with the taxonomy.** For example, this could require certain firms to report the share of revenue, capital expenditure and/or operational expenditure that is aligned with the taxonomy. This would help investors better align their investments with their sustainability objectives and help regulators to consistently assess sustainability claims made by firms. It will also provide a foundation for more rigorous transition planning and reporting, by providing a consistent means of tracking and demonstrating how sustainability performance and alignment is improving over time.
* **Requiring financial entities to disclose the degree of alignment of their investment products or portfolios with the taxonomy**. This could strengthen the development of an investment product labelling regime, enabling consumers to better understand the sustainability characteristics of products and funds, and providing a stronger foundation for regulatory oversight.

There are a number of ways to embed the taxonomy into regulatory arrangements and market practices in Australia:

* The taxonomy could be given **legislative force** by including the underlying criteria in legislation. This would support establishing clear mandatory reporting requirements against the taxonomy criteria, consistent with the planned approach to legislating mandatory disclosure of climate-related financial opportunities and risks.
* Financial regulators formally adopting the **taxonomy as a standard or framework** to guide their supervisory and enforcement activities – for example, by actively encouraging reporting against the taxonomy on an “if not, why not” basis. This would set clear expectations for firms and investment managers to embed taxonomy criteria in their products and processes, or to provide a clear justification for why they have departed from it.
* Alternatively, the taxonomy could be used as part of a **voluntary best practice guide** or framework issued by regulators.

It is likely that a legislative approach will give more force to the taxonomy’s use cases, provide clearer guidance to markets, and ensure that the taxonomy is an effective foundation of the Government’s sustainable finance agenda. However, while the Government will consider these options in the medium-term, a taxonomy will not be directly incorporated into regulatory architecture for financial reporting or product labelling unless and until the Government is satisfied that Australian taxonomy criteria are credible, internationally-aligned, readily useable by financial market participants and will materially support the development of Australia’s sustainable finance products, markets and capabilities.

**Permanent governance arrangements**

The taxonomy will be a key foundation for the Government’s sustainable finance agenda. It will need to be maintained and evolve to reflect changes in technology, policy and market factors. It will also need to be seen as a credible part of Australia’s financial market infrastructure and be aligned with broader sustainability policy objectives.

To achieve these outcomes, the taxonomy should be overseen and maintained by an appropriate government body or agency once the initial phase of taxonomy development is complete. Such a function would need to ensure there is sufficient expertise and knowledge on taxonomies, data and the financial system. This is to ensure the taxonomy remains up to date and useable as sustainable finance markets evolve, new sustainability targets are set, the economy progresses towards net zero and Australia becomes a renewable energy superpower.

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| For feedback   * What are the most important policy priorities and use cases for an Australian sustainable finance taxonomy? What are the key insights from international experience to date? * What are priorities for expanding taxonomy coverage after the initial focus on climate mitigation objectives in key sectors? * What are appropriate long-term governance arrangements to ensure that the taxonomy is effectively embedded in Australia’s financial and regulatory architecture? |

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| Box 4: International regulatory use cases of taxonomies  The following are examples of regulatory use-cases for taxonomies in other jurisdictions:  **Provide metrics for firms to report against to indicate sustainability alignment of their revenue, investment portfolio, financial products.** The **EU’s Taxonomy Regulation** supports disclosures against both the Corporate Sustainability Reporting Directive and the Sustainable Finance Disclosure Regulation. In practice, this requires firms and financial institutions to disclose how their revenues, activities and financial products and portfolios are aligned with taxonomy criteria. **Singapore’s Green Finance Industry Taskforce** has suggested this as a possible use case for Singapore’s taxonomy. Singapore’s approach is to develop the taxonomy as a voluntary tool which can be used by various stakeholders for a range of purposes.  **Develop and regulate an investment product labelling system.** The **UK’s Financial Conduct Authority** is consulting on a regime for labels for investment products, aimed at addressing greenwashing, which could link to the UK Green Taxonomy (under development) as a means to demonstrate sustainability credentials.  **Classifying eligible green and transition activities to support the issuance of green or transition-aligned financial instruments, including bonds and loans**. Canada’s Sustainable Finance Action Council has recommended this as a use case for a potential Canadian taxonomy.  **Support macroprudential regulators in understanding risks to financial system stability that may stem from “unsustainable” activities per the taxonomy.** Singapore’s Green Finance Industry Taskforce outlines this as a possible use case.  **Serve as the basis for determining ESG ratings by ratings agencies.** This is a potential use-case considered under the Association of Southeast Asian Nations (ASEAN) Taxonomy. |

## Priority 3: Support credible net zero transition planning

Given the systemic and long-term nature of climate change, transition planning is a uniquely important component of an organisation’s overall business strategy. Transition planning includes setting firm-level emissions targets and developing approaches to manage the physical and transition risks associated with climate change, forming part of effective corporate decision-making and management. Credible and effective transition plans can provide vital signals to markets and support effective near- and long-term capital allocation decisions. It is therefore important that transition *planning* is undertaken effectively, and that transition *plans* are disclosed accurately.

Many firms and financial institutions have announced net zero emissions targets and have begun to publicly disclose their transition plans and strategies. In Australia, nearly 75 per cent of the ASX 200 by market capitalisation is now covered by firm-level net zero commitments.[[2]](#footnote-3) Globally, financial institutions with over US$150 trillion in assets or funds under management have made net zero commitments under the Glasgow Financial Alliance for Net Zero (GFANZ) banner.

In recent years there has been greater regulatory and policy focus on the credibility and transparency of transition plans. The new ISSB climate disclosure standards include requirements for firms to disclose firm-level targets and transition plans, and the OECD, IPSF, G20 and GFANZ have all published guidance on corporate climate transition planning.The Government is closely monitoring the work of the Transition Plan Taskforce (TPT) in the UK, which recently published a detailed transition plan disclosure framework and sector-specific guidance. Despite progress on these global initiatives, there is still considerable variation in how corporate transition planning is undertaken and disclosed – making it more difficult for firms to set plans and track progress, and harder for investors to allocate capital to support the transition.

This is a particular challenge and priority in Australia, where many of our largest firms and financial institutions face significant transition opportunities and risks. Supporting more transparent, credible and ambitious transition planning and disclosure by Australian firms is a key medium-term priority for the Government. Australia’s approach will be built around introduction of globally-aligned climate disclosure requirements, development of more regulatory and practical guidance, and medium-term investment tools and capabilities that will enable good transition planning and reporting.

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| Proposed approach  Australia’s corporate transition plan disclosure requirements will be contained in the proposed requirements for large companies and financial institutions to disclose climate-related opportunities and risks.  Following the finalisation of Australian disclosure standards, ASIC will inform the market of its key expectations and supervisory priorities relating to the disclosure of transition-related targets, plans and claims. These will be informed by emerging international standards and practice.  Treasury will consult with industry and other stakeholders to consider broader priorities and options for strengthening transition planning. The intent will be to develop high quality, internationally-aligned transition planning practices and reporting requirements, to better inform markets and support the flow of transition finance. |

In line with ISSB standards, the Government’s proposed mandatory disclosure requirements will require transition plans to be disclosed, including information about climate-related targets and progress towards these targets, and any mitigation strategies. The ISSB standard provides a framework for disclosing specific transition plan information, including how resource allocation decisions are responsive to climate risks, the intended use of carbon offsets, and how progress against plans will be monitored. A focus on transparency at this level is expected to drive entities towards greater ambition in response to market demands. Additional ASIC guidance will support the implementation of these new requirements, drawing on international best practice.

To complement this focus on disclosure, the Government is accelerating and coordinating investments in other policy frameworks that will support credible transition planning by firms, financial institutions and investors. These include:

* The development of national **sectoral emissions reduction pathways** as part of Australia’s 2050 Net Zero Plan. These will provide firms and investors with clearer policy guidance on anticipated emissions reductions trajectories and priorities in key sectors, supporting more rigorous corporate transition planning and increasing accountability.
* The development of the **sustainable finance taxonomy** sustainability objectives. This will provide a consistent set of metrics for firms and investors to set targets and track and demonstrate their progress on sustainability impacts and performance.

The Government does not intend to introduce transition planning disclosure requirements that go beyond ISSB-aligned standards in the near term. Immediate priorities will be to focus on the smooth introduction of new climate disclosure requirements, and to work with industry and investors to identify opportunities to support credible transition planning and disclosure. This will provide an opportunity to assess how sectoral pathways, taxonomy and other frameworks can play a role as part of a ‘building blocks’ approach to supporting better transition planning in the medium-term.

In 2024, Treasury will work with the CFR to provide updated recommendations on further steps to enhance firm level transition planning, beyond ISSB-aligned disclosure requirements. This will consider whether additional regulatory requirements to promote transparent and credible transition planning are needed, and what further tools, resources and guidance can support best practice transition planning by Australian firms and financial institutions. In undertaking this work, the CFR will consider the final design of the Australian disclosure regime, the broader Australian climate policy landscape, and emerging international standards and practices.

The Government will consider responses to this consultation before finalising a near-term position on transition planning disclosure requirements or additional guidance.

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| For feedback   * What are key gaps in Australian capability and practice, including relative to ‘gold standard’ approaches to transition planning developed through the TPT and other frameworks? * To what extent will ISSB-aligned corporate disclosure requirements improve the transparency and credibility of corporate transition planning? What additional transition disclosure requirements or guidance would be most useful in the medium-term? * Are there related priorities and opportunities for supporting enhanced target setting and transition planning for nature and other sustainability issues? |

## Priority 4: Develop a labelling system for investment products marketed as sustainable

The market for sustainable investment products is expanding. An estimated $1.3 trillion worth of financial assets in Australia are managed using a ‘responsible’ investment approach.[[3]](#footnote-4) However, a wide range of investment approaches are marketed as ‘sustainable’ or similar, and it can be difficult for investors to understand how these investments are managed or to verify their sustainability characteristics. Different approaches include:

* Integrating sustainability considerations into investment decision-making processes alongside other factors. ‘Sustainability’ or ‘ESG’ integration is now becoming a routine practice for active asset managers looking to manage risk and maximise returns.
* Adopting ‘screening’ strategies which restrict the universe of assets that a fund can hold. This can involve excluding certain exposures (e.g. fossil fuels) or focusing specifically on a particular investment theme (e.g. renewable energy).
* Designing financial products that aim to make a specific non-financial impact, tailored for investors looking to align their capital directly with specific environmental or social outcomes.

While investment product issuers are subject to extensive disclosure obligations, the diversity of the sustainable finance landscape can be confusing for investors. There are voluntary certifications and standards that provide a degree of consistency and assurance, including the long-running Responsible Investment Association of Australia Certification Program which has been widely adopted in Australia and New Zealand. However, without a consistent regulatory approach, it is difficult for investors to understand how sustainability considerations are factored into investment products and strategies.

This lack of clarity and the limited ways to verify that investments are true to label can contribute to greenwashing, erode credibility in the sustainable finance market and ultimately result in a misallocation of capital. Investors have indicated that a lack of both understanding and trust are key barriers to the growth of sustainable investment markets.

In response to these trends, financial regulators in major global capital markets are developing new labelling and disclosure frameworks for financial products and funds. This includes major reforms currently being introduced or developed in the United States, the United Kingdom, and the European Union (see Box 5) to establish consistent labels and disclosure requirements for sustainable products. Informed by developments in other jurisdictions, the Government intends to develop a sustainable investment labelling regime to strengthen arrangements in Australia. This will provide better information to consumers and investors, provide regulatory clarity that supports ASIC’s ability to address greenwashing, and help align Australian financial markets with global peers.

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| Proposed approach  The Government will legislate to create a labelling regime for investment products marketed as ‘sustainable’ or similar, including for managed funds and within superannuation. Treasury will commence work on this reform in 2024, consulting closely with regulators and industry stakeholders on policy and legislative design. |

The proposed labelling regime will seek to introduce labels for the primary purpose of informing retail investors of the sustainability characteristics of different investment products. While they would also benefit from clearer labelling arrangements, institutional investors would not be a specific focus of the reforms, as they have a comparably greater understanding of the sustainable finance market and greater capacity to scrutinise sustainability claims.

The Government intends to standardise the use of sustainability terminology in investment product marketing by setting minimum standards for what qualifies for a prescribed sustainability label. To promote comparability across the financial system, the regime will cover all sustainable investment products marketed to retail investors, including managed investment scheme products and superannuation investment options. Funds that integrate sustainability into investment processes without an explicit sustainability objective would not qualify for a label.

Under this approach, investment product issuers would also be required to provide retail investors with additional information on sustainable investment products, both pre-contractually and on a periodic basis. This would include a description of how sustainability is incorporated into the investment process.

Treasury will commence implementation of these reforms in 2024. The process will involve detailed consultation with industry, analysis of international approaches and consideration of existing industry standards and practices in Australia. The Government will also assess the possible integration of other sustainable finance frameworks, such as the taxonomy.

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| For feedback   * What should be the key considerations for the design of a sustainable investment product labelling regime? * How can an Australian model build off existing domestic approaches and reflect key developments in other markets? |

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| Box 5: International developments in investment product labelling  The **European Union** has implemented a Sustainable Finance Disclosure Regulation (SFDR), which imposes disclosure obligations for investment funds that incorporate sustainability. Most funds in the European Union fall under either ‘Article 8’ (funds that promote ESG characteristics) or ‘Article 9’ (sustainable investment is an objective). To provide further regulatory clarity, the European Securities Market Authority (ESMA) is consulting on fund labelling guidelines.  The **United Kingdom’s Financial Conduct Authority (FCA)** is consulting on a framework of labels and disclosure requirements for sustainable investment products. The FCA proposed three labels: ‘sustainable focus’, ‘sustainable improvers’ and ‘sustainable impact’. Funds would need to qualify for a label to be marketed as ‘sustainable’ or similar.  The **Securities and Exchange Commission (SEC) in the United States** has proposed a framework for classifying ESG funds, with graduated disclosure obligations. The proposed labels cover ‘integration funds’, ‘ESG-focused funds’ and ‘impact funds’. ‘Integration funds’ would not be permitted to market themselves as ‘ESG’ or similar. |

# Pillar 2: Financial system capabilities

Enhanced transparency is central to the integration of sustainability in financial markets and economic decision making. However, for opportunities and risks to be managed effectively, transparency alone is not enough – sustainability-related considerations need to be practically embedded in the decision making and governance of firms, financial institutions and regulators.

Driven by commercial realities, sustainability is already becoming a key consideration for financial market participants seeking to manage risks and position themselves for long-term success. Financial regulators are prioritising climate and sustainability issues and identifying how these intersect with their existing regulatory mandates and frameworks. Firms and financial institutions have developed new disciplines for integrating these issues into sound corporate risk management and governance. There has been considerable investment across the economy to build the new sustainability-related resources, data systems and expertise.

The Government is seeking to support this momentum, to ensure that financial institutions and markets are well positioned to tackle long-term sustainability challenges.

This section identifies three priorities for strengthening financial sector capabilities and governance practices:

* Equipping Australia’s financial regulators to address key sustainability priorities, including increasing sustainability-related **market supervision and enforcement** and deepening analysis of **sustainability-related systemic risks and responses**.
* Supporting work across government to address **data challenges and priorities** that are most important for firms and institutions to better understand and manage sustainability issues.
* Ensuring that **regulatory frameworks for sustainability governance** are fit for purpose in key sectors and across the economy – ensuring that sustainability priorities can be properly factored in and managed by Australian investors and institutions.

Reforms in these areas will ensure firms, financial institutions and regulators can strengthen their sustainability-related capabilities, and that our data, governance and regulatory frameworks position Australia to be a leader in green and sustainable finance.

## Priority 5: Enhancing market supervision and enforcement

Transparency-related measures across the proposed Sustainable Finance Strategy will support ASIC in its core role to regulate corporations, markets and financial services. Mandatory climate disclosure requirements will provide transparent and comparable climate-related information across financial markets and will support ASIC’s ability to scrutinise claims made by regulated entities. Other reforms, including the sustainable finance taxonomy and investment product labels, will set clear regulatory expectations and strengthen ASIC’s ability to promote transparency and respond to misconduct.

These new frameworks will support ASIC to build on its efforts in recent years to promote the appropriate integration of sustainability considerations into financial markets, consistent with an increasing focus on climate and sustainability by global peer regulators. Since 2019, clear ASIC guidance on the disclosure of material climate risks and the TCFD framework have supported steady improvement in the quality and consistency of climate-related disclosures in Australia.

ASIC has developed an enhanced regulatory focus on greenwashing. In 2022, ASIC issued guidance on *How to avoid greenwashing when offering or promoting sustainability-related products* and indicated that misleading conduct in relation to sustainable finance, including greenwashing, is one of its 2023 enforcement priorities. ASIC has recently made several regulatory interventions on greenwashing matters involving listed companies, superannuation funds and managed funds, reinforcing strong expectations that sustainability claims must be accurate and substantiated.

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| Proposed approach  The Government will continue to support ASIC’s capacity to supervise and address market misconduct as it relates to sustainable finance, including to target greenwashing, building on additional resourcing provided to ASIC to accelerate this work in 2023-24. |

The Government supports ASIC’s focus on sustainable finance, including to target greenwashing, and will ensure ASIC is appropriately resourced in this area. The Government provided ASIC with an additional $4.3 million in 2023‑24 to enhance its sustainable finance related surveillance and enforcement action, allowing ASIC to continue its expanded supervisory and enforcement focus on greenwashing and invest in its wider sustainability-related expertise and capabilities.

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| For feedback   * Are Australia’s existing corporations and financial services laws sufficiently flexible to address greenwashing? What are the priorities for addressing greenwashing? * Is there a case for regulating ESG ratings as financial services? |

While the Government regards current legislative settings as being generally sufficiently flexible to address misconduct in sustainable finance markets, it is open to feedback on regulatory gaps and priorities. This could include regulation of ESG ratings providers, which have been subject to proposals in other jurisdiction to improve transparency. The Government will consider feedback on whether ESG ratings should be captured by financial services regulation, comparably to credit ratings agencies.

## Priority 6: Identifying and responding to potential systemic financial risks

The physical impacts of climate change and the global transition to net zero will have far reaching economic impacts. These issues are being increasingly recognised in terms of their impact on financial institutions and financial system stability. Analytical work by financial regulators and international organisations is building on scientific knowledge to better understand the financial impacts of climate change. However, there remains considerable uncertainty around how opportunities and risks will affect financial institutions, and about potential system-wide impacts of climate shocks and trends.

Improving our understanding of climate-related financial impacts will help financial institutions and regulators respond effectively, protecting financial system participants and promoting broader financial stability. Government and regulators also need to strengthen their understanding of broader sustainability risks, including nature-related risks which are being increasingly recognised by market participants as having potentially significant macroeconomic and financial implications.

Improved disclosure of sustainability-related risks, impacts and plans by firms and financial institutions will provide a stronger foundation for monitoring and responding to system-wide trends and potential vulnerabilities. However, Government and financial regulators will need to take additional steps to develop a comprehensive understanding of systemic risks and coordinate regulatory responses.

The CFR Climate Working Group was established in 2017 to coordinate regulators’ response to climate-related financial risks, including at the systemic level. The Australian Prudential Regulation Authority (APRA) has led the CFR’s efforts to better understand how climate-related financial risks affect banks, insurers and superannuation funds. This included leading the first stage of the CFR’s Climate Vulnerability Assessment, which measured the potential physical and transition climate risks of climate change faced by the major banks and highlighted the value of collaboration between financial institutions and regulators to identify and manage these risks. The Working Group has played an influential role increasing awareness and understanding of climate risks in Australia and it is important this momentum continues.

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| Proposed approach  Led by APRA, the CFR will continue to expand its work on climate- and sustainability-related financial risks, deepening risk management capabilities and practices across financial regulators and market participants.  This will include applying the CFR’s Climate Vulnerability Assessment process to undertake a climate scenario analysis focused on the household insurance sector. |

APRA will continue to deepen its understanding of climate-related financial risks faced by regulated entities. This will include engaging with financial institutions to understand their climate-related governance and risk management processes, such as how climate scenarios are incorporated into stress testing processes. Globally, APRA is an engaged member of the Network of Central Banks and Supervisors for Greening of the Financial System (NGFS), alongside the Reserve Bank of Australia (RBA). APRA is also working with other agencies and industry to better understand climate-related risks, including by participating in the Hazards Insurance Partnership managed by the National Emergency Management Agency. This public-private process is analysing physical climate risks and insurer responses.

In addition to APRA’s work on climate-related financial risks, complementary work is underway across the other CFR agencies. For example:

* The RBA considers how climate change affects the economy and the financial system as part of its monetary policy and financial stability responsibilities. The recent review of the RBA supported continued integration of the implications of climate change into the RBA’s analysis and modelling.
* The Government has restored Treasury’s capability to model climate opportunities and risks. This will allow Treasury to assess the economic impacts of domestic and global climate change mitigation and adaptation policies, and climate damages on the Australian economy, supporting a more consistent and detailed whole-of-government assessment of climate risk.

As these analytical capabilities develop, Treasury and the CFR will work together to ensure that modelling processes and methodologies are aligned where possible and that there is a coordinated, whole-of-government approach to assessing systemic financial and macroeconomic risks.

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| For feedback   * Are there specific areas where the Government or regulators could further contribute to market-wide understanding of systemic sustainability related risks, including climate-related financial risks? |

## Priority 7: Addressing data and analytical challenges

Sustainability data is an increasingly important input in financial decision-making. The availability and accuracy of relevant metrics and data enables investors and institutions to assess opportunities and risks, make effective and accurate disclosures, and work towards sustainability targets.

However, the sustainability data landscape is evolving and complex. While a range of data is collected and published by the Government and companies, specialist private-sector providers also play an important role to develop datasets, ratings tools and analytical resources. This has resulted in an array of innovative data solutions and products that support climate capabilities for firms, financial institutions and regulators. It has also created challenges due to a proliferation of tools, methods and standards which can be fragmented and opaque. The cost and complexity of accessing reliable data and expertise is also a challenge, especially for smaller entities.

Data-related challenges faced by both firms and investors were highlighted in Treasury’s initial consultation on new mandatory climate disclosure requirements. Stakeholders noted important gaps in data and capability, particularly around scope 3 emissions reporting and scenario analysis. The significance of these challenges has been recognised across other jurisdictions, and there are coordinated efforts to address them through the Financial Stability Board (FSB), the G20’s Sustainable Finance Working Group and other international processes.

Addressing the full range of data challenges, gaps and opportunities that are relevant to climate and sustainability is beyond the scope of this Strategy. However, the Government is seeking feedback on the highest priority data challenges to support sustainable finance.

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| Proposed approach  To address climate- and sustainability-related data challenges, the Government will continue to work with investors and industry stakeholders to ensure new sustainable finance tools and frameworks are well adapted to the needs of investors and markets.  The Government is seeking feedback on sustainability data challenges and priorities for financial system participants, with a particular focus on what is necessary to support effective corporate risk disclosure, informed financial decision-making and effective transition planning.  Building on this feedback, the Treasurer will request that the CFR conducts a detailed assessment of options to address key sustainability-related data challenges faced by financial system participants. The CFR will publish recommendations to Government by the end of 2024. |

The Government is taking several key steps to improve the availability and quality of sustainability-related data in areas that are critical to informed financial sector decision-making. Examples include:

* Improving **data sources and analytical tools in priority sectors**. For example, the Government is expanding and upgrading the Nationwide Household Energy Rating Scheme (NatHERS) to apply to existing homes. Enhanced data on the energy efficiency of houses will improve lenders’ understanding of their financed (scope 3) emissions and facilitate lending for the purpose of improving the energy efficiency of borrowers’ homes.
* Strengthening the **measurement of natural capital**, including as part of the National Strategy for Environmental Economic Accounting. Natural capital data frameworks will enhance assessments of nature-related opportunities and risks by financial institutions.
* Investing in **high quality climate information and services**, one of the four agreed roles of the Commonwealth Government in climate adaptation. This includes strengthening provision of physical climate risk information, including through the National Climate Risks Assessment by the Australian Climate Service in an updated Statement of Expectations and by the CSIRO, to support informed investment decisions in the financial sector.

The Government is also seeking feedback on a wider range of data challenges and opportunities to prioritise as part of the CFR assessment. Issues highlighted in initial stakeholder engagement include:

* The estimation of scope 3 emissions in large and complex supply chains, sectors or portfolios.
* Consistent and accessible understanding of climate scenarios and decarbonisation pathways across economies, sectors and industries, and how they affect individual sectors or firms.
* Access to reliable and comparable sustainability data beyond emissions (e.g. physical climate impacts and on nature-related risks and impact).
* The availability of corporate sustainability data, including the potential value of a centralised repository and the utility of data reported in a standardised, digital format.

Informed by feedback received in this consultation process, the Treasurer will request that the CFR assess key sustainability data gaps and priorities from a financial system perspective and provide key recommendations to Government on how these could be addressed. This will involve coordination with the CER, Australian Bureau of Statistics, Australian Climate Service and other agencies as required, as well as consultation with stakeholders in the financial sector and real economy. The CFR’s analysis and recommendations will be considered by the Government as part of its system-wide efforts to strengthen climate and sustainability data. The Treasurer will ask that the CFR publish its recommendations to Government by the end of 2024.

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| For feedback   * What are the priorities for ensuring that data-related initiatives already underway are tailored to meet the needs of firms and investors? * What key sustainability data gaps or uncertainties faced by financial institutions in Australia should be prioritised by the CFR? |

## Priority 8: Ensuring fit for purpose regulatory frameworks

To be fit for the long-term, the legal and regulatory frameworks that govern the decision-making and mandates of companies, financial institutions and regulators must enable and ensure proper consideration of climate change and other sustainability-related issues. Improving understanding of opportunities and risks is not enough if decision makers are unclear about how their legal duties permit or require them to consider climate-related issues, or if they cannot effectively communicate how and why sustainability factors are being incorporated into governance processes alongside other priorities.

In recent years, existing principles-based frameworks for corporate governance have adapted well to these issues, especially where sustainability trends or issues represent clear-cut financial opportunities and risks. It is now widely accepted that climate and sustainability matters can be material to the financial prospects of a company or the financial interests of investors. Company directors’ duties to act in the best interests of the company enable, and in many circumstances require, directors to actively integrate sustainability considerations into corporate decision-making and governance.

For financial institutions, climate-related risks are likely to manifest through a variety of conventional channels such as loan defaults, insured losses, and re-pricing of assets. Managing these risks is part of sound risk management practice, underpinned by clear legislative and regulatory expectations. Consistent with their existing mandates, financial regulators in Australia have set strong expectations regarding the relevance of sustainability risks within existing regulatory frameworks concerning corporate conduct, prudential risk and financial stability. For example:

* ASIC has explicitly recognised that climate change is a systemic risk that could have a material impact on the future financial position, performance or prospects of entities,reinforcing obligations for companies to properly consider and disclose climate risks.[[4]](#footnote-5)
* APRA has issued guidance on managing the financial risks of climate change within the existing prudential framework,to practically assist banks, insurers and superannuation trustees to manage the financial risks of climate change.[[5]](#footnote-6) It has also provided guidance on investment management for superannuation trustees on how sustainability risk factors should be considered by funds, as part of their overall investment risk management processes.[[6]](#footnote-7)

Overall, Australia’s regulatory and governance frameworks are well-positioned to manage sustainability issues and trends, supported by the Government’s actions to enhance transparency, capabilities and policy frameworks. However, the Government is seeking to ensure that these frameworks remain fit-for-purpose as the impacts of climate change and related policy responses evolve.

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| Proposed approach  The Government will continue to work with financial regulators, governance experts and industry stakeholders to identify policy priorities for mainstreaming sustainability considerations in corporate governance and financial institution decision-making, including taking into account stakeholder feedback from this consultation process.  In the area of superannuation and managed funds, the Government will assess how regulatory frameworks or industry codes can support effective investor stewardship as a tool to promote long-term corporate performance that contributes to positive sustainability outcomes. |

**Financial regulation frameworks**

The Government has supported financial regulators’ work to integrate sustainability considerations, consistent with their existing legislative mandates. In June 2023, the Government updated its *Statement of Expectations* for APRA to prioritise the promotion of prudent practices and transparency in relation to climate-related financial risks.

Feedback received in this consultation will inform APRA’s approach to providing regulated entities with more specific guidance on how they should approach managing climate-related risks. The Government is also open to broader feedback on the possible longer-term direction of prudential policy frameworks in the face of climate change and other sustainability risks. This could include views on reforms proposed or discussed in other jurisdictions.[[7]](#footnote-8)

The Government is also seeking feedback on potential enhancements to regulatory frameworks which could further integrate consideration of sustainability-related opportunities and risks by companies, financial institutions and regulators. This could include priorities for clarifying how sustainability considerations should be integrated into decision making by companies and specific classes of financial institutions (including banks, insurers, superannuation funds and other managed funds).

**The superannuation system**

As part of these considerations, the Government is seeking views on options and priorities for enhancing the ability of institutional investors, especially superannuation funds, to play a role in supporting the transition to net zero, consistent with the best financial interests of their members.

The Government’s recent *Your Future, Your Super Review* (YFYS) underscored the importance of the performance test to hold trustees to account for member returns. The performance test will apply to trustee‑directed products for the 2023 testing period, increasing the number of products subject to performance testing. The Government has announced fine-tuning changes for the 2023 test following feedback received from the YFYS review. To encourage long-term investment approaches, including investment in the transition to net zero, the Government will extend the performance test lookback period from eight to ten years. Key benchmarks will also be calibrated to ensure that funds are not unintentionally discouraged from investing in certain assets. The Government will continue to explore and consult on further changes that improve the sophistication of the test to scrutinise underperformance across superannuation products.

**Investor stewardship**

One further specific area of focus is frameworks supporting investor stewardship, which refers to the active exercise of asset ownership rights to advance the long-term interests of beneficiaries. Investor stewardship is a routine part of corporate governance processes in Australia and is becoming an increasingly prominent aspect of sustainable finance. Many large investors and asset owners are actively engaging with companies to encourage and support the transition away from emissions‑intensive activities, and voluntary codes such as the industry-led Australian Asset Owner Stewardship Code seek to support a consistent approach to stewardship activities.

There are no explicit barriers to stewardship in the Australian market, and wider reforms in sustainable finance will provide further support and guidance to asset owners. However, some stakeholders are seeking further clarity on how Government and regulators expect stewardship to be undertaken and disclosed. The Government is seeking feedback on reforms that could support more effective and transparent investor stewardship in Australia, including for superannuation trustees and collective investment fund operators respectively.

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| For feedback   * Do you agree that existing regulatory and governance frameworks and practices have adapted well to support better integration of sustainability-related issues in financial decision making? Are there barriers or challenges that require further consideration? This may include:   + **Corporate governance** obligations, including directors’ duties   + **Prudential frameworks and oversight**, including in relation to banks and insurers   + Regulation of the **superannuation system** and **managed investment schemes** * What steps could the Government or regulators take to support effective investor stewardship? |

# Pillar 3: Australian Government leadership and engagement

Clear government commitments, policies and strategies are crucial to aligning private sector investment with sustainability goals for both domestic and international investors. Strong public policy frameworks provide the signals and certainty that Australian firms and financial institutions need to invest with confidence and effectively allocate capital for the long-term. Effective international engagement on climate and sustainability-related issues is a critical enabler for cross-border sustainable finance flows, as global investors and capital markets weigh up Australia’s attractiveness as a destination for green investment in a competitive global market.

The Government has taken major steps to ensure this strong environment for investment domestically. These include legislating Australia’s net zero target and 2030 emissions reductions commitment, developing a Net Zero 2050 plan which includes sectoral decarbonisation plans for six key sectors, enshrining independent progress reporting and oversight by the Climate Change Authority, delivering a clear framework for emissions reductions in industry through the Safeguard Mechanism, introducing the $20 billion Rewiring the Nation program to accelerate Australia’s clean energy transformation, and establishing the Net Zero Authority to drive the transformation. The Government has also invested in catalysing growth of key sustainable finance products and markets through special investment vehicles like the Clean Energy Finance Corporation. These climate-focused measures have been supported by a host of other commitments and reforms, including major investments and targets for nature repair, biodiversity and other pressing sustainability issues.

Internationally, Australia has significantly stepped up its engagement on climate and sustainability. As an open and globally integrated economy, Australia’s ability to mobilise the private sector investment needed to support net zero, become a renewable energy superpower and achieve other sustainability goals hinges on our ability to tap into sustainability‑conscious international capital flows and markets, and on the success of global efforts to combat climate change. Further, as a key economic player in the Indo‑Pacific, Australia can benefit from, and support, sustainable finance flows as climate adaptation and decarbonisation reshape trade and investment, build resilience and security, and create major new economic opportunities across our region. Australia’s strong and stable financial system, respected regulators, sophisticated investors and significant sustainability-related capabilities and opportunities mean we have a lot to offer, even as we build on initial steps that have been pioneered elsewhere, such as the sustainable finance taxonomy.

There are opportunities to build on this proactive and targeted government leadership and engagement to deepen and expand our sustainable finance markets and crowd in the private investment critical to realising the transition to net zero. This section identifies four priorities for strengthening government leadership and engagement on sustainable finance:

* Developing an Australian **sovereign green bonds program** to attract green capital and support further growth of sustainable finance markets.
* Promoting **interoperability** of sustainable finance frameworks to enable cross-border flows of sustainable finance.
* Catalysing growth of **key sustainable finance products and markets**, especially in sectors where rapid scaling up of sustainable investment is a key policy priority.
* Leveraging international engagement on sustainable finance and blended finance commitments **to position Australia as a global sustainability leader.**

## Priority 9: Issuing Australian sovereign green bonds

Rapid growth in green and sustainable debt markets has been a key trend in global sustainable finance in recent years. Surging issuance of sustainability-themed debt products is helping to mobilise sustainability-aligned capital, deepen sustainability-related capabilities and expertise, and to develop more sophisticated and liquid sustainable finance products and markets.

Sovereign bond issuance has been an important part of this trend. Since Poland issued the first sovereign green bond in 2016, more than 40 countries have followed suit, as well as a host of sub-sovereign jurisdictions. These include the United Kingdom, Germany, France, Canada, New Zealand and Indonesia, with more than US$350 billion in sovereign green bonds now on issue. In Australia, Victoria, Queensland, New South Wales and Western Australia have begun green bond programs.

A well designed and credible sovereign green bond program can mobilise additional climate-aligned capital, deepen sustainable finance markets and signal a government’s commitment to climate, energy and other sustainability-related goals. With a much stronger array of climate and sustainability targets and policies now in place, and wider reforms to support sustainable finance underway, Australia is well-placed to join international peers and commence a sovereign green bond program.

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| Proposed approach  The first issuance of the Government’s sovereign green bond program is expected in mid-2024. |

Issuing sovereign green bonds is an important step to signal Australia’s commitment to accelerating sustainable finance and supporting the net zero transformation. This will help attract more green capital to Australia, by increasing transparency around climate outcomes and the scale of green investments available. It will also support Australia’s wider green capital markets to mature and scale.

The Australian Office of Financial Management (AOFM) will be issuing green bonds. Treasury has commenced work with AOFM and other government agencies to develop a Green Bond Framework. Treasury will engage with climate and nature policy experts, state and international counterparts, and investors and financial market participants to develop a high-quality green bond program and work with the market ahead of first issuance in 2024.

Over time, green bonds are expected to support projects that address climate change mitigation and adaptation, along with natural resources depletion, loss of biodiversity and air and water pollution.

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| For feedback   * What are the key expectations of the market around issuance of, and reporting against, sovereign green bonds? What lessons can be learned from comparable schemes in other jurisdictions? * What other measures can the Government take to support the continued development of green capital markets in Australia? |

## Priority 10: Catalysing sustainable finance flows and markets

As well as supporting wider foundations for sustainable investment, the Government can play a catalytic role to promote the development sustainable financial products, practices and markets.

Over the past decade the Clean Energy Finance Corporation – the largest government-owned green bank in the world – has worked alongside investors, innovators and industry to drive emissions reductions and sustainable investment across our economy. As well as financing large-scale investments in emissions reductions, the CEFC has worked through financial institutions to provide discounted loans and finance for clean energy projects across agriculture, industry, property and transport. It has also spearheaded the development of new sustainability-aligned financial markets and products, supported development of innovative investment products, and provided guidance to investors to help assess emerging sustainable technologies and opportunities.

The CEFC continues to be at the forefront of the Government’s efforts to drive Australia’s energy transformation, including as financing agent to deliver the $20 billion Rewiring the Nation program. As sustainable finance markets and practices become more mature, the CEFC will also continue to have a key role backing innovative products, technologies and financing models and the development of new standards, frameworks and practices that can drive sustainable investing into the mainstream.

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| Proposed approach  The CEFC will support the delivery of the Government’s sustainable finance strategy by expanding its discounted financing across priority sectors and market segments, contributing to the development phase of the sustainable finance taxonomy, and contributing to the development phase of energy assessment tools (such as NatHERS In-Homes) for financial product applicability and consistency with sustainable finance best practice. |

The CEFC was allocated $1 billion in the 2023-24 Budget to provide discounted consumer finance across the housing sector, working alongside banks and other financial institutions. The new Household Energy Upgrades Fund will support investment in energy efficiency upgrades, high performing appliances and battery-ready solar PV. This builds on the CEFC’s well-established model of supporting clean energy investments for households and SMEs, and expands its focus on the housing sector, which is a key priority for expanding sustainable finance and reducing Australia’s emissions.

The CEFC will also support the development of clear standards and frameworks that can boost growth and integrity of sustainable finance products and markets. This will include supporting the initial development phase for an Australian Sustainable Finance Taxonomy, with a particular focus on sustainability metrics and criteria for the housing and property sector, as well as providing expert advice to the CFR as it oversees this work. The CEFC’s expertise, including in asset-level classification of energy decarbonisation technologies and the development of sustainable finance standards, can also support the development of the Commonwealth’s sovereign green bond framework.

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| For feedback   * What role can the CEFC play to support scaling up of sustainable investment in Australia, as part of a more comprehensive and ambitious sustainable finance agenda? * What are the key barriers and opportunities for the CEFC to support financing and market development in areas with significant climate co-benefits, including nature and biodiversity? |

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| Box 6: Key initiatives for Government sustainable finance leadership  Several other initiatives are underway in Treasury and other agencies to drive major uplift in sustainability-related coordination and expertise across government. These will support delivery of the Sustainable Finance Strategy and establish new frameworks and capabilities to improve sustainability outcomes and policy in the long term.  **Strengthening coordination on sustainable finance across financial regulators and states & territories**   * Since 2017, the CFR Climate Working Group has coordinated regulatory responses to climate-related financial risks. * The Council of Federal Financial Relations has recently established a sustainable finance work stream to examine public sector disclosure frameworks and support new approaches to transition planning.   **Engaging with investors domestically and globally**   * The Treasurer is holding Investor Roundtables bringing together leaders from Australia’s largest financial institutions. Past topics have included energy and sustainable finance. * Treasury, the AOFM and other agencies are stepping up engagement with global institutional investors.   **Collaboration and coordination to drive net zero investment and transformation in our regions**   * The Government has established the Net Zero Economy Agency to promote orderly and positive economic transformation.   **New approaches to measuring wellbeing and long-term outcomes**   * The Government’s Measuring What Matters statement outlined Australia’s progress against key sustainability indicators.   **Accelerating net zero momentum and leadership across the APS**   * The Government has committed to net zero emissions in the APS by 2030.   **Supporting a circular economy**   * In 2023, a Circular Economy Ministerial Advisory Group was established by the Minister for the Environment and Water.   **Scaling up climate modelling capability and long-term risk assessments**   * The Government has provided nearly $30 million to expand Treasury’s climate modelling capability. * The 2023 Intergenerational Report included in-depth analysis of physical impacts of climate change and the transition to net zero. * The Government is undertaking a Climate Risk Assessment to better understand the risks and impacts to Australia from climate change. |

## Priority 11: Promoting international alignment

As global momentum on sustainable finance has accelerated, a range of new processes and frameworks have emerged to promote best practice and establish new standards. While this offers potential to harmonise practices and unlock critical new sources of investment, the risk of fragmentation is also creating challenges for firms trying to navigate new rules, build new capabilities and operate across multiple jurisdictions. Policymakers need to develop frameworks that are suitable for their markets, while also minimising compliance costs and complexities that may result from divergences with global frameworks.

Australia has significantly elevated its international engagement on sustainable finance in recent years, with a focus on supporting global frameworks that can promote consistent global approaches (see Box 7). Supporting a consistent global approach also means ensuring that global frameworks can cater effectively to the issues that are most relevant for Australia’s economy and our region. Given the importance of transition finance for Australia and the Indo-Pacific, Australia has advocated strongly for global sustainable finance frameworks to include a sophisticated approach to transition finance, and is actively contributing to technical work to support consistent approaches across jurisdictions.

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| Proposed approach  Australia will continue to support the development of consistent global standards, and seek to maximise alignment of sustainable finance frameworks across different jurisdictions.  Multilateral engagement will be complemented by a scaled-up focus on bilateral and regional mechanisms to promote knowledge sharing, capability development and interoperability. |

Australia has laid strong foundations to promote alignment of sustainable finance frameworks through bilateral relationships, and global and regional fora, such as ASEAN. As new frameworks such as the ISSB standards and sustainable finance taxonomies mature, focusing on practical measures to support consistency and interoperability across different markets and jurisdictions will be very important to promote cross-border sustainable finance flows. Maximising consistency between tools such as taxonomies will mean investors can more easily assess whether activities and investments in other markets are aligned with their own strategies and with regulatory requirements in their home jurisdiction. This reduces compliance costs and opens up new opportunities for investment.

Priority issues in the next phase of Australia’s bilateral and regional engagement will include supporting approaches to transition finance frameworks that are adapted to the needs of our region, and supporting two-way knowledge sharing and capability-building as regional economies adopt new international frameworks like the ISSB climate and sustainability disclosure standards. This will support strong sustainable finance networks and partnerships across the region, helping to meet demands for greater transparency and investment in economies that need to mobilise larger sustainable finance flows, and creating more opportunities for Australian firms to invest in the wider region’s transition.

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| For feedback   * What are the key priorities for Australia when considering international alignment in sustainable finance? |

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| Box 7: Stepping up Australia’s global engagement on sustainable finance Multilateral **G20 Sustainable Finance Working Group:** Australia is a strong supporter of the G20’s Sustainable Finance Roadmap, of which key elements include the central role of the ISSB standards for climate disclosures, developing sustainable finance markets, and identifying levers to mobilise capital for the transition.  **International Platform on Sustainable Finance:** In December 2022, Australia joined this major global forum for harmonisation of sustainable finance policies and best practice. Members include the EU, India, China, the UK, and Indonesia. Critical streams of work in the IPSF include the development of a common ground taxonomy and increased focus on transition finance.  **Coalition of Finance Ministers for Climate Action:** The Treasurer joined this key international forum in 2021. Active workstreams include transparency, climate finance, and transition.  **Taskforce for Nature-Related Financial Disclosures:** Australia has been a strategic funding partner for the TNFD, with the Government and Australian entities actively participating in a pilot phase the Government’s wider focus on nature related finance.  **Global Nature Positive Summit:** Australia will host the Global Nature Positive Summit in 2024 to help drive private investment for on-the-ground nature repair and protection. The Summit aims to support other countries attract private investment in nature.  **The United Nations Framework Convention on Climate Change and the Paris Agreement:**Australia is supporting activities to align finance with pathways for low emissions and climate-resilient development, including through our membership on the [Standing Committee on Finance](https://unfccc.int/SCF) and our participation and facilitation of expert dialogues which will underpin the design of the [New Collective Quantified Goal](https://unfccc.int/NCQG) on climate finance, due for decision in 2024.  **Other:** The Government also participates in sustainable finance agendas through other groupings, including the OECD, IMF, and APEC, with Australia’s financial regulators actively engaged in the FSB, International Organisation of Securities Commissions (IOSCO) and NGFS. Bilateral and regional **Singapore-Australia Green Economy Agreement:** The GEA covers a range of matters relevant to sustainable finance, in particular green and transition finance, and offers a model for cooperation with other regional partners to support the region’s transition to net zero. Concrete deliverables include technical exchanges on sustainable finance taxonomies and data priorities.  **Australia-New Zealand 2+2 Climate and Finance Dialogue:** Sustainable finance is a key component of this dialogue with one of our closest partners, with a commitment to align of our sustainable finance frameworks and tools to enhance interoperability and support businesses.  **Australia Indonesia Climate and Infrastructure Partnership:** A $200 million initiative focused on increasing sustainable finance flows into Indonesia through blended finance mechanisms along with policy and regulatory support.  **Indo-Pacific Economic Framework:** Australia is actively engaged in discussions on incentives and tools to enable the transition to net zero across the members (which includes the US), with a strong focus on collaboration and interoperability in approaches to sustainable finance. |

## Priority 12: Position Australia as a global sustainability leader

Sustainable finance is an increasingly important feature of the global response to climate change and a critical avenue for countries to demonstrate climate ambition, credentials and commitment. As a resource-intensive advanced economy with deep and globally integrated financial markets, and major climate transition and adaptation opportunities and risks, other countries may look to Australia as an important example of how sustainable finance can support whole-of-economy responses.

Further, Australia, as an advanced economy in the Indo-Pacific region with a sophisticated investment sector, is in a position to promote and enhance private sector financing for the transition to net zero and other sustainability priorities in our region. The challenges of financing are complex, and intersect with other economic and development priorities. For example, balancing significant decarbonisation with energy security and access is a focus in Southeast Asia, with estimates in 2021 that the ASEAN region would need at least US$367 billion over the next five years to finance its energy plans.[[8]](#footnote-9) Public sector institutions, including governments and multilateral development banks, have a crucial role to play in this context.

Through elevated international engagement on climate and sustainable finance, and significantly enhancing Australia’s commitments to blended finance and other innovative financing for sustainability in our region, Australia is positioning itself as a committed partner and leader on sustainability and global climate action. There is now an opportunity for Australia to build on this momentum and ensure that Australian firms, industries, and investment opportunities are viewed favourably by global partners and markets.

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| Proposed approach  Building on a more coordinated and ambitious Sustainable Finance Strategy, the Government will promote sustainable finance as key pillar of ambitious international engagement on climate and nature, helping to position Australia as a regional and global leader in sustainability.  Australia will continue to support innovative financing models and approaches, including blended finance models, to support sustainable investment in our region. This will complement the expansion of direct Government-led financing efforts to support regional sustainability priorities. |

Clear and credible leadership on sustainable finance will enhance Australia’s status as a destination for sustainable finance and investment and attract international capital needed to help drive our transition. Further, it would support future opportunities such as co-hosting COP31 in conjunction with Pacific neighbours by demonstrating Australia’s global ambition and commitments on climate and sustainable finance. Such an opportunity could also help draw in greater focus on the pressing climate financing needs of Pacific nations, and encourage more action on sustainable finance for climate issues that generally attract less engagement and funding, such as adaptation. This would then place Australia in a much stronger international position to help shape discussions on sustainability, particularly on key issues such as transition finance, nature and biodiversity, and a just transition.

International leadership and continued support of blended financing for sustainable investment will also provide opportunities to influence global and regional developments around transition, climate solutions and nature in the Indo-Pacific. Australia is scaling up its contribution to blended finance and other innovative financing mechanisms in the region. The 2023-24 Budget lifted the financial cap of Australia’s Emerging Markets Impact Investment Fund from $40 million to $250 million, greatly enhancing Australia’s capacity to support blended finance solutions and technical assistance to help unlock financing for SMEs in the Indo-Pacific region.[[9]](#footnote-10) This builds on expanded investment in the October 2022-23 Budget in climate infrastructure through grants and concessional financing from the Australian Infrastructure Financing Facility for the Pacific. The Government has also released its International Development Policy and the Development Finance Review conducted by the Department of Foreign Affairs and Trade, accepting all eight recommendations. The recommendations include establishing Australian Development Investments, a vehicle providing up to $250 million for private impact investment in the Indo-Pacific.

Looking ahead, in addition to scaling up the overall quantum of Australia’s blended finance aimed at climate solutions in the Indo-Pacific, it will be important to ensure that blended finance and investment vehicles take a robust approach to sustainability. This includes both mainstreaming sustainability considerations, as well as credible frameworks for assessing and choosing sustainable activities to support. Taking an innovative approach would also require consideration of new types of blended finance. In particular, those aimed at the types of projects that are hard to finance, such as smaller-scale, SME-focused, projects in least developed countries,[[10]](#footnote-11) as well as new mechanisms to open up flows of private investment toward sustainable activities.

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| For feedback   * What are other key near-term opportunities for Australia to position itself as a global leader in sustainable finance and global climate mitigation and adaptation? * What are some longer-term international sustainability goals for Australia where sustainable finance can play a role? * What are the key market, regulatory and institutional barriers to increasing private sector engagement in blended financing opportunities? How can these barriers be overcome? * What are other means to mobilise private sector finance toward sustainability solutions in the Indo-Pacific region? |

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